

Message Text

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ACTION MMO-04

INFO OCT-01 ARA-14 ISO-00 AID-05 CIAE-00 EB-08 FRB-01
INR-10 NSAE-00 ICA-20 TRSE-00 XMB-04 OPIC-06
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07
CEA-01 AGRE-00 ITC-01 INT-05 DOE-15 SOE-02 /132 W
-----061517 181722Z /43

R 142040Z APR 78
FM AMEMBASSY BUENOS AIRES
TO USDOC WASHDC
INFO SECSTATE WASHDC 5358

UNCLAS SECTION 1 OF 2 BUENOS AIRES 2862

C O R R E C T E D C O P Y (PARA 4)

PASS EXIMBANK

E.O. 11652: N/A
TAGS: ECRP,AR
SUBJECT: CERP-0006; TRADE OUTLOOK REPORT

REF: A) 77 BA-3545; (B) CERP-0004 FOREIGN ECONOMIC TRENDS
ARGENTINA, JANUARY 78

1. SUMMARY: THE ARGENTINE ECONOMY IS CURRENTLY EXPERIENCING
A RECESSION, BUT ECONOMIC ACTIVITY IS EXPECTED TO RECOVER
TO NORMAL LEVELS DURING THE COURSE OF 1978. INVESTMENT IS
PROJECTED TO REACH 24 PERCENT OF GNP IN 1978 AND SHOULD
BE A STIMULUS TO ECONOMIC RECOVERY. FOREIGN EXCHANGE
RESERVES ARE AT AN ALL TIME HIGH - US\$5 BILLION, OVER A
YEAR'S IMPORTS. ARGENTINA SHOULD AGAIN HAVE A SIZEABLE
BALANCE OF PAYMENTS SURPLUS THIS YEAR. CAPITAL GOODS IMPORTS
ARE LIKELY TO CONTINUE AT 1977'S RECORD LEVELS, STIMULATED BY
THE AVAILABILITY OF RESERVES AND THE LOWERING OF TARIFF AND
NON-TARIFF BARRIERS. PROSPECTS ARE GOOD, THEREFORE, FOR US
EXPORTERS OF CAPITAL GOODS TO ARGENTINA, WHERE A NUMBER OF
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MAJOR PROJECTS IN THE HYDROELECTRIC, MINING, COMMUNICATIONS,
PETROCHEMICAL, PULP AND PAPER AND STEEL SECTORS ARE IMMINENT.
THE TERRORIST THREAT HAS BEEN GREATLY REDUCED IN ARGENTINA TODAY,
AND SECURITY FOR BUSINESSMEN IS NOT THE OVERRIDING CONSIDERA-
TION IT ONCE WAS.

2. THE PERFORMANCE OF THE ECONOMY. AFTER RECOVERING NICELY

IN 1977 FROM THE RECESSION OF 1975 AND 1976, THE ARGENTINE ECONOMY BEGAN TO SLUMP AGAIN IN THE THIRD QUARTER OF DECEMBER 1977, FOLLOWING A GOVERNMENT DECISION TO COOL DOWN THE ECONOMY, WHICH WAS OVERHEATING AND THREATENING TO REVERSE THE DECLINING TREND OF INFLATION. IN APRIL 1978, THE LEVEL OF ACTIVITY IS STILL CONSIDERABLY BELOW NORMAL. IT APPEARS THAT BY A COMBINATION OF RESTRICTIVE MONETARY POLICY AND HIGH INTEREST RATES THE GOA HAS SUCCEEDED ALL TOO WELL IN ITS GOAL OF COOLING THE ECONOMY-PROBABLY TO A GREATER EXTENT THAN THEY INTENDED. NEVERTHELESS, INTEREST RATES HAVE DECLINED SUBSTANTIALLY RECENTLY AND THERE PRESENTLY SEEMS TO BE NO OTHER MAJOR OBSTACLE TO RECOVERY THAN DEPRESSED DEMAND. REVIVING DEMAND COULD, HOWEVER, PROVE DIFFICULT, AS THE GOVERNMENT CANNOT, OR WILL NOT, APPLY FISCAL STIMULATION IN VIEW OF ITS ANTI-INFLATIONARY POLICY, WHICH HAS FIRST PRIORITY. IT IS POSSIBLE THAT RECOVERY WILL BE LED IN THE FINAL ANALYSIS BY INVESTMENT SPENDING, WHICH IS PROJECTED AT ABOUT 12 PERCENT OF GNP FOR EACH OF THE PUBLIC AND PRIVATE SECTORS IN 1978. IT WAS THIS SECTOR WHICH WAS RESPONSIBLE IN 1977 FOR A GOOD DEAL OF THE BOYANCY OF THE ECONOMY (GROSS FIXED INVESTMENT TOTALLED 20.4 PERCENT IN THIS YEAR). AS IT IS LIKELY THAT THERE WAS A DROP IN GROWTH DURING THE FIRST QUARTER, (FOLLOWING A 4.4 PERCENT INCREASE IN GNP FOR 1977), OFFICIAL PROJECTIONS FOR A GNP GROWTH RATE OF 5 PERCENT IN 1978 SEEM OVERLY OPTIMISTIC. GNP IS NOT LIKELY TO GROW MORE THAN 2 PERCENT THIS YEAR. A 5 PERCENT, OR HIGHER, RATE OF GROWTH IN 1979, IS MORE LIKELY.

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3. FOREIGN EXCHANGE RESERVES AT ALL TIME HIGH. GROSS FOREIGN EXCHANGE RESERVES ARE CURRENTLY PAST THE US\$ 5 BILLION MARK-OVER A YEAR'S IMPORTS. THE YEAR IS EXPECTED TO CLOSE WITH A TRADE SURPLUS OF APPROXIMATELY US\$750 MILLION AND A BALANCE OF PAYMENTS SURPLUS OF 1.7 BILLION. THE TRADE SURPLUS IS LESS THAN LAST YEAR'S (US\$ (1.7 BILLION) LARGELY BECAUSE THE WHEAT CROP AND WHEAT EXPORTS ARE EXPECTED TO BE OFF CONSIDERABLY THIS YEAR BECAUSE OF LESS FAVORABLE CLIMATIC CONDITIONS AND BECAUSE PRICES AT THE TIME OF PLANTING WERE NOT VIEWED AS PARTICULARLY STIMULATING BY THE ARGENTINE FARMER. THOUGH THE DECLINE IN WHEAT EXPORTS WILL BE COMPENSATED TO SOME EXTENT BY INCREASED EXPORTS OF CORN AND OTHER FARM PRODUCTS, THE RECORD LEVELS OF AGRICULTURAL EXPORTS OF 1977 WILL NOT BE REPEATED.

4. 1978 IMPORTS. IT IS DIFFICULT TO DETERMINE WHETHER IMPORTS AS A WHOLE WILL INCREASE SIGNIFICANTLY IN FY 1978 GIVEN AN ASSUMPTION OF 2 PERCENT GROWTH OF GNP. THERE WILL PROBABLY BE MODEST GROWTH AND TOTAL IMPORTS MAY REACH US\$ 4.4 BILLION COMPARED TO US\$4.2 BILLION IN 1977. THIS PROJECTION IS BASED ON A NUMBER OF FACTORS: RESERVES ARE AT AN ALL TIME HIGH, TARIFF BARRIERS CONTINUE TO BE REDUCED SUBSTANTIALLY (THE AVERAGE

DUTY ON MACHINERY FOR EXAMPLE, HAS GONE FROM ABOUT 90 PERCENT TO 50 PERCENT IN THE PAST YEAR AND A HALF), IMPORT LICENSING REGULATIONS ARE GREATLY SIMPLIFIED, THE GOA'S EXCHANGE RATE POLICY CONTINUES TO FAVOR IMPORTS AS THE DOLLAR BECOMES PROGRESSIVELY CHEAPER, AND, FINALLY, ARGENTINE INDUSTRY CONTINUES TO REQUIRE A SIGNIFICANT AMOUNT OF REPLACEMENT OF EXISTING EQUIPMENT WHICH IS TECHNICALLY OUTDATED AND WORN OUT. THE PINCH OF FOREIGN COMPETITION PROMOTED BY THE LOWERING OF TARIFF BARRIERS SHOULD GIVE LOCAL INDUSTRY AND ADDITIONAL REASON TO WANT TO REPLACE OUTDATED MACHINERY. THIS POINT OF VIEW IMPLIES THAT CAPITAL GOODS IMPORTS WILL AT A MINIMUM REMAIN AT LAST YEAR'S LEVELS, THE HIGHEST IN RECENT ARGENTINE HISTORY: US\$1.073 BILLION.

5. PROSPECTS FOR SALE OF MACHINERY AND EQUIPMENT. IN THE CAPITAL
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GOODS CATEGORY, BEST SALES PROSPECTS FOR US FIRMS OVER THE NEXT YEAR ARE LIKELY TO BE IN THE FOLLOWING AREAS:

- 1) MACHINE TOOLS
- 2) POWER GENERATION AND TRANSMISSION
- 3) PETROCHEMICAL PLANT EQUIPMENT
- 4) HEAVY CONSTRUCTION AND MINING EQUIPMENT
- 5) COMMUNICATIONS EQUIPMENT
- 6) OILFIELD EQUIPMENT
- 7) PULP & PAPER MILL MACHINERY
- 8) STEELMAKING EQUIPMENT

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ACTION MMO-04

INFO OCT-01 ARA-14 ISO-00 AID-05 CIAE-00 EB-08 FRB-01
INR-10 NSAE-00 ICA-20 TRSE-00 XMB-04 OPIC-06
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07
CEA-01 AGR-01 ITC-01 INT-05 DOE-15 SOE-02 /133 W
-----046723 171700Z /47

R 142040Z APR 78
FM AMEMBASSY BUENOS AIRES
TO USDOC WASHDC
INFO SECSTATE WASHDC 5359

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THESE ARE THE SECTORS IN WHICH THERE ARE MAJOR INVESTMENT PROJECTS PENDING AT THE MOMENT. A SAMPLING OF THESE PROJECTS INCLUDES:

A) US\$3.5 BILLION HYDROELECTRIC PROJECT AT YACIRETA-APIPE ON THE PARANA RIVER, WHERE CONSTRUCTION SERVICES, EARTHMOVING EQUIPMENT AND ELECTROMECHANICAL SALES ARE POSSIBLE.

B) A US\$1 BILLION COOPER MINING PROJECT PLANNED BY ST. JOSEPH'S MINERALS IN SAN JUAN PROVINCE, WHICH WILL REQUIRE EARTHMOVING, SMELTING AND MINING EQUIPMENT.

C) CONTRACTS FOR SEVERAL HUNDRED MILLION DOLLARS OVER THE NEXT FIVE YEARS TO UPGRADE ARGENTINA'S COMMUNICATIONS SYSTEM BY INSTALLING NEW TELEPHONE SWITCHING EQUIPMENT, TELEX MODEMS, EXPANDING THE MICROWAVE NETWORK, AND INSTALLATION OF COAXIAL CABLES.

D) EXPANSION OF RURAL ROAD NETWORK THROUGH A US\$105 MILLION WORLD BANK LOAN, WHICH WILL REQUIRE PURCHASING OF A CONSIDERABLE AMOUNT OF ROAD CONSTRUCTION EQUIPMENT BY LOCAL CONSTRUCTION FIRMS.
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E) A US\$400 MILLION PETROCHEMICAL COMPLEX CONSTRUCTION PROJECT, WHICH WILL INCLUDE A PVC PLANT, LOW AND HIGH DENSITY POLYETHYLENE PLANTS, A VCM PLANT EXPANSION OF THE EXISTING ETHYLENE PLANT, A CAPROLACTAM PLANT AND A PHENOL-ACETONE PLANT.

F) AN INDUSTRIALIZATION PROJECT FOR SMALL AND MEDIUM FIRMS BANK CREDIT.

G) THE CONSTRUCTION OF A GAS PIPELINE BETWEEN NEUQUEN AND SANTA FE PROVINCES. COMPRESSORS WILL BE NEEDED FOR THIS PIPELINE.

H) A LARGE COPPER MINING PROJECT AT BAJO DE LA ALUMBRERA IN CATAMARCA PROVINCE, PROMOTED BY FABRICACIONES MILITARES, THE ARMED FORCES INDUSTRIAL COMPLEX.

I) WOOD PROCESSING EQUIPMENT FOR A PULP MILL TO BE SET UP IN MISIONES PROVINCE BY CELULOSA ARGENTINA, WITH APPROXIMATELY US\$70 MILLION IN IMPORTED EQUIPMENT.

J) CONSTRUCTION OF A BLAST FURNACE (WORTH ABOUT US\$10 MILLION) FOR A STEEL MILL IN CHACO PROVINCE BY THE FIRM TAMET.

6. RELAXATION OF IMPORT BARRIERS. Z.U.S. EXPORTERS SHOULD PAY CLOSE ATTENTION TO THE DRASTIC DECLINE IN TARIFF RATES APPLICABLE PARTICULARLY TO MACHINERY AND INTERMEDIATE GOODS WHICH HAS OCCURRED IN ARGENTINA OVER THE PAST YEAR. NOT ONLY HAVE TARIFF LEVELS BEEN REDUCED ON MOST ITEMS, BUT FOR MACHINERY WHICH IS NOT PRODUCED LOCALLY, RATES IN MANY CASES WILL GO DOWN AS LOW AS 10 PERCENT AFTER JULY 1978. THIS IS TRUE
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OF EQUIPMENT IN BTN CHAPTERS 84 AND 85 WHICH INCLUDES THE FOLLOWING CATEGORIES: GENERATORS, MOTORS, FOOD PROCESSING MACHINES, CONSTRUCTION AND MATERIALS HANDLING EQUIPMENT, MACHINE TOOLS, OFFICE MACHINERY ELECTRIC MACHINES. ADDITIONALLY, IMPORT LICENSING PROCEDURES FOR ALL TYPES OF GOODS IN GENERAL, HAVE BEEN GREATLY SIMPLIFIED. IN FACT, IMPORT APPROVAL TODAY IS ALMOST AUTOMATIC. THE CENTRAL BANK HAS RECENTLY AGAIN RELAXED THE TERMS WHICH IMPORTERS MUST OBTAIN FOR THE FINANCING OF CAPITAL GOODS IMPORTS. THE VALUE OF GOODS WHICH CAN ENTER WITHOUT FINANCING HAS BEEN RAISED FROM \$50,000 TO \$250,000. IN ADDITION, THE UPPER VALUE LIMIT OF IMPORTS WHICH CAN ENTER UNDER A 5-YEAR REPAYMENT SCHEDULE WITHOUT NECESSITATING SPECIAL ARRANGEMENTS APPROVED BY THE CENTRAL BANK HAS BEEN INCREASED FROM \$2 MILLION TO \$5 MILLION.

7. THE ARGENTINE GOVERNMENT HAS SUBSTANTIALLY REDUCED THE EFFECTIVENESS OF TERRORIST GROUPS IN ARGENTINA WHICH IMPINGED SO HEAVILY ON BUSINESS ACTIVITIES HERE.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: CERP, TRADE, CERP 0006
Control Number: n/a
Copy: SINGLE
Draft Date: 14 apr 1978
Decaption Date: 01 jan 1960
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01 jan 1960
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978BUENOS02862
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D780169-0644, D780164-0355
Format: TEL
From: BUENOS AIRES
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t19780456/aaaabvbn.tel
Line Count: 260
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 0aa601b0-c288-dd11-92da-001cc4696bcc
Office: ACTION MMO
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 5
Previous Channel Indicators: n/a
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 29 mar 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: N/A
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 2965380
Secure: OPEN
Status: NATIVE
Subject: CERP-0006; TRADE OUTLOOK REPORT
TAGS: ECRP, AR
To: COM
Type: TE
vdkgvwkey: odbc://SAS/SAS.dbo.SAS_Docs/0aa601b0-c288-dd11-92da-001cc4696bcc
Review Markings:
Sheryl P. Walter
Declassified/Released
US Department of State
EO Systematic Review
20 Mar 2014
Markings: Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014